

5-1-1970

# Tight-Money Real Estate Financing and the Florida Usury Statute

Seneca B. Anderson

Follow this and additional works at: <http://repository.law.miami.edu/umlr>

---

## Recommended Citation

Seneca B. Anderson, *Tight-Money Real Estate Financing and the Florida Usury Statute*, 24 U. Miami L. Rev. 642 (1970)  
Available at: <http://repository.law.miami.edu/umlr/vol24/iss3/8>

This Leading Article is brought to you for free and open access by Institutional Repository. It has been accepted for inclusion in University of Miami Law Review by an authorized administrator of Institutional Repository. For more information, please contact [library@law.miami.edu](mailto:library@law.miami.edu).

# TIGHT-MONEY REAL ESTATE FINANCING AND THE FLORIDA USURY STATUTE

SENECA B. ANDERSON\*

I. INTRODUCTION .....	642
II. IMPORTANCE OF AVOIDING JURY ISSUES .....	643
III. THE FOUR ELEMENTS OF USURY .....	645
IV. IS THERE A LOAN? .....	645
V. THE SALE-LEASEBACK: IS IT A DEVICE TO EVADE USURY OR A LEGITIMATE ALTERNATIVE TO A LOAN? .....	648
A. <i>The Sale-Leaseback without Repurchase Agreements, Repurchase Options,         or Other Frills</i> .....	649
B. <i>The Sale-Leaseback Where the Seller Must Repurchase</i> .....	650
C. <i>The Sale-Leaseback with an Option to Repurchase</i> .....	651
D. <i>The Leaseback with a Leasehold Mortgage</i> .....	653
VI. THE FLORIDA RULE ON ACCELERATION AND USURY .....	658
VII. PITFALLS FOR THE UNWARY .....	660
VIII. METHODS OF AVOIDING USURY .....	663
A. <i>Requiring the Borrower to Incorporate: Avoidance not Evasion</i> .....	664
B. <i>Use of Mortgage Bonds</i> .....	668
C. <i>Contracting for the Law of Another Jurisdiction</i> .....	669
IX. CONCLUSION .....	671

## I. INTRODUCTION

Until recently, reputable lenders, such as banks and life insurance companies, did not find it necessary to concern themselves in more than a casual way with the Florida usury statute. Unlike some states which imposed a limit on interest of six percent per annum, Florida set its permissible annual rate at fifteen percent for corporate loans and ten percent for loans to individuals and noncorporate entities.<sup>1</sup> Since the going rate was substantially below ten percent, usury was almost never involved in loans made by institutions specializing in first mortgages on prime properties.

Now that interest rates have risen to approximately ten percent per annum<sup>2</sup> and life insurance companies are aggressively seeking participation in equity positions as a condition to lending money on first mortgages at any rate of interest, Florida lawyers are called upon to advise these institutions whether their "New Look in Real Estate Financing"<sup>3</sup> runs afoul of our usury statute. The harsh and inflexible pen-

---

\* B.A. 1930, Louisiana State University, LL.B. 1933, Harvard University. Member of the Tennessee, Massachusetts, and Florida bars; partner in the Miami law firm of Shutts and Bowen.

1. FLA. STAT. §§ 687.02-.03 (1967).

2. Miami Herald, Jan. 6, 1970, § B, at 4, col. 1.

3. Defined by Mandes Hershman, Associate General Counsel of The New York Life Insurance Company, as: "[M]ortgagee (investor) participation in entrepreneurial profits and the corresponding leverage for the mortgagor (developer) of a small equity position through high ratio financing." *Usury and the New Look in Real Estate Financing*, 4 REAL PROP., PROBATE & TRUST J. 315 (1969).

alties<sup>4</sup> accompanying any violation discourage the financing of Florida real estate developments unless the institutions providing the money can be assured of the legality of their investments. It is the purpose of this article to review the Florida statute, the Florida cases, and occasionally cases from other jurisdictions, in an attempt to arrive at some guidelines by which lenders may be governed.

## II. IMPORTANCE OF AVOIDING JURY ISSUES

Since jurors are more likely to be drawn from the debtor than the creditor class, those who seek a high rate of return on their investments can expect little consideration before such jurors. Hence, it is vital that the lawyer urge such clients as banks and life insurance companies to beware of situations where the determination of usury may depend on a disputed question of fact. Ideally, the investor should be in a position to obtain a summary judgment or directed verdict should usury be raised.

If a genuine issue of material fact seems possible, the client should be so informed because if there is such an issue, the trier of fact, which can be a jury, must make a determination.<sup>5</sup> Even if the facts are undisputed, there can still be a jury question if conflicting inferences can be drawn therefrom;<sup>6</sup> otherwise, there is only an issue of law for the

---

4. These penalties have recently been reduced but are still severe. Fla. Laws 1965, ch. 65-299, now incorporated in FLA. STAT. § 687.11 (1967), was followed by Fla. Laws 1969, ch. 69-135, which became effective October 1, 1969. These acts are analyzed by the supreme court in *Tel Serv. Co. v. General Capital Corp.*, 227 So.2d 667 (Fla. 1969). Forfeiture of both principal and interest, which applied to criminal usury (where annual interest was willfully and knowingly charged in excess of 25 percent), was terminated on October 1, 1969, thus providing honorable burial to the body of Florida law distinguishing between criminal and civil usury. At the present time (January, 1970), the sole penalty for a usurious loan to a corporation is forfeiture of all interest. FLA. STAT. § 687.11 (1967). The same penalty applies to an individual in the case of interest willfully charged, but where usurious interest is willfully taken, reserved, or paid, the lender forfeits all unpaid interest and double the interest actually collected or taken from the noncorporate borrower. FLA. STAT. § 687.04 (1967). The reason for the double penalty is that where interest is actually paid, the debtor has to take affirmative action to recover it; whereas if he only contracts for it, he can avoid payment by merely interposing usury as a defense. *Wilson v. Connor*, 106 Fla. 6, 142 So. 606 (1932). The penalties are not discretionary. If a transaction is tainted with usury, the courts must apply them. *Hormuth v. Dickson*, 115 Fla. 790, 156 So. 127 (1934); *River Hills, Inc. v. Edwards*, 190 So.2d 415 (Fla. 2d Dist. 1966). The amount of any interest taken or contracted for above the maximum is immaterial. Even two days' additional interest has been held to taint a loan with usury. *Maxwell v. Jacksonville Loan & Imp. Co.*, 45 Fla. 425, 34 So. 255 (1903).

5. *Bess v. 17545 Collins Ave., Inc.*, 98 So.2d 490 (Fla. 1957); *Goff v. Miami Transit Co.*, 77 So.2d 636 (Fla. 1955).

6. *Bruce Constr. Corp. v. The State Exch. Bank*, 102 So.2d 288 (Fla. 1958); *Gravette v. Turner*, 77 Fla. 311, 81 So. 476 (1919). In the *Bruce* case, the court quoted the following from the *Gravette* case:

Where there is room for a difference of opinion between reasonable men as to the proof of facts from which an ultimate fact is sought to be established, or where there is room for such differences as to the inferences which might be drawn from conceded facts, the court should submit the case to the jury, as it is their conclusion, in such cases, that should prevail, and not primarily the views of the judge. *Id.* at 291.

judge. If the judge is also the trier of fact,<sup>7</sup> he applies the law to the facts as he finds them, but his findings of fact are entitled to the same weight as a jury verdict.<sup>8</sup> If there is a jury, the judge instructs its members as to the relevant law and they apply it to the facts as they find them. There is not necessarily a genuine issue just because the parties disagree on material facts. It is not the function of the judge to weigh the evidence, but he must decide whether there is such conflict in the evidence as would cause reasonable men to believe the issue to be in doubt.<sup>9</sup> If he decides that there is, the case goes to the jury; if he decides there is not, he grants summary judgment or directs a verdict.

The foregoing points up the responsibility of the attorney toward the financial institution. He must recognize that in a suit involving the question of usury, the opposing party and his client may differ as to one or more facts, especially those concerning the client's intent. Before his client's transaction is closed, the lawyer must exercise his judgment and determine whether there is a substantial likelihood that, in case a claim of usury is made, enough credible evidence adverse to his client's claims of fact can be produced to require the judge to submit the issue to the jury. Such an exercise of judgment is a proper function of the attorney, although attempting to predict how the jury will decide the facts, once they are submitted to it, definitely is not. Therefore, he should limit his opinion to a statement of what he finds the law to be and his estimate of the risk that a genuine issue of material fact could be raised which might be submitted to a jury. This is very different from attempting to predict a jury's verdict. If the client elects to assume such a risk of jury trial thus pointed out by his attorney, the attorney should, at the very least, accumulate and preserve evidence which will minimize the possibility of an adverse finding of fact.

---

7. Most Florida cases involving usury are foreclosure suits, where usury is raised as a defense. As these were formerly suits in equity and not actions at law, the Chancellor, as the circuit judge was called in such suits, rather than the jury, was the trier of fact. Nevertheless, in an appreciable number of the reported decisions, the borrower initiated the litigation by suing the lender to recover the penalties imposed by the statute. *E.g.*, *Tel Service Co. v. General Capital Corp.*, 227 So.2d 667 (Fla. 1969); *Holland v. Gross*, 89 So.2d 255 (Fla. 1956); and *Chakford v. Sturm*, 65 So.2d 864 (Fla. 1953). These actions by the borrower were formerly at law; thus the borrower has a constitutional right to trial by jury. Hence, the fact that most usury cases are decided by a judge without a jury should not lull the lender into believing that his transaction will be scrutinized by a judge alone. Any borrower threatened with foreclosure may secure a jury trial by anticipating the lender and suing first. He can also obtain a jury by counterclaiming in an equity action. *See Hightower v. Bigoney*, 156 So.2d 501 (Fla. 1963).

8. *Hall v. Adams*, 155 Fla. 1, 19 So.2d 412 (1944); *Lake Towers, Inc. v. A.T. Euster Furn. Co.*, 174 So.2d 448 (Fla. 3d Dist. 1965).

9. *Bruce Constr. Corp. v. The State Exch. Bank*, 102 So.2d 288 (Fla. 1958); *Gravette v. Turner*, 77 Fla. 311, 81 So. 476 (1919). In *Zampos v. United States Smelting, Refining and Min. Co.*, 206 F.2d 171, 174 (10th Cir. 1953), the court said: "And flimsy allegations which are transparently not well founded in fact are insufficient to state a justiciable controversy requiring the submission thereof for trial." We may therefore conclude that while the judge must refrain from weighing the evidence, he is not required to assume a posture of complete gullibility.

### III. THE FOUR ELEMENTS OF USURY

Usury is an affirmative defense<sup>10</sup> which must be proven by clear and satisfactory evidence.<sup>11</sup> The Florida courts on more than one occasion<sup>12</sup> have stated that there are four elements in a usurious transaction, each of which must be established. First, there must be a loan, express or implied; second, an understanding between the parties that the money loaned is to be returned; third, payment or agreement to pay a greater rate of interest than is allowed by law; and, finally, a corrupt intent to take more than the legal rate for the use of the money loaned.

### IV. IS THERE A LOAN?

In most cases where A borrows money from B, the nature of the transaction is evident. Sales with repurchase options<sup>13</sup> and even some sales with repurchase agreements<sup>14</sup> have been held not to be loans, although there are many instances of loans being disguised in these forms.<sup>15</sup> The determining factor is intent.<sup>16</sup> Since both the legislature

10. *Yaffee v. International Co.*, 80 So.2d 910 (Fla. 1955).

11. *Brumick v. Morris*, 131 Fla. 46, 178 So. 564 (1938); *Benton v. Wilkins*, 118 Fla. 491, 159 So. 518 (1935); *Cutri Enterprises, Inc. v. Pan-American Bank*, 115 So.2d 592 (Fla. 2d Dist. 1959).

12. *Clark v. Grey*, 101 Fla. 1058, 132 So. 832 (1931); *Stewart v. Nangle*, 103 So.2d 649 (Fla. 2d Dist. 1958); *Diversified Enterprises, Inc. v. West*, 141 So.2d 27 (Fla. 2d Dist. 1962); *Lord v. Hodge*, 209 So.2d 692 (Fla. 2d Dist. 1968). But the loan must be a loan of money. Thus, in *Davidson v. Davis*, 59 Fla. 476, 52 So. 139 (1910), the court said:

The law is well settled that usury can only attach to a loan of money, or to the forbearance of a debt, and that on a contract to secure the price or value of work and labor done, or to be done, or of property sold, the contracting parties may agree upon one price if cash be paid, and upon as large an addition to the cash price as may suit themselves if credit is given; and it is wholly immaterial whether the enhanced price be ascertained by the simple addition of a lumping sum to the cash price, or by a percentage thereon. In neither case is the transaction usurious. It is neither a loan nor the forbearance of a debt, but simply the contract price of work and labor done and property sold; and the difference between cash and credit in such cases, whether 6, 10 or 20 per cent., must be left exclusively to the contract of the parties, and no amount of difference fairly agreed upon can be considered illegal.

*Id.* at 478, 52 So. 139.

13. *Rosenthal v. Le May*, 72 So.2d 289 (Fla. 1954); *Zmistowski v. Oxley*, 161 So.2d 706 (Fla. 2d Dist. 1964).

14. *B & D, Inc. v. E-Z Accept. Corp.*, 186 So.2d 29 (Fla. 3d Dist. 1966); *Indian Lake Estates, Inc. v. Special Inv., Inc.*, 154 So.2d 883 (Fla. 2d Dist. 1963).

15. *Mears v. Mayblum*, 96 So.2d 223 (Fla. 1957); *Maxwell v. Jacksonville Loan & Imp. Co.*, 45 Fla. 425, 34 So. 255 (1903); *Kay v. Amendola*, 129 So.2d 170 (Fla. 2d Dist. 1961).

16. From time to time, the Florida courts have more or less unsuccessfully attempted to explain what they mean by a corrupt intent to charge usury. See *Dezell v. King*, 91 So.2d 624 (Fla. 1956); *Chandler v. Kendrick*, 108 Fla. 450, 146 So. 551 (1933); The best explanation this writer has seen is contained in Shanks, *Practical Problems in the Application of Archaic Usury Statutes*, 53 VA. L. REV. 327, 341 (1967):

The required intention is not a subjective one to violate the usury laws, nor even to enter into a loan transaction in excess of the legal maximum. All that is required is an intention to do the acts that constitute a loan of money in excess of the legal maximum. The parties may be blissfully unaware of the usury laws or they may honestly believe their transaction is not, in legal contemplation, a loan. However,

and the courts have recognized that lenders will resort to schemes and devices to cloak usury with the appearance of legitimacy, it is important to establish what the courts will find, as a matter of law, not to be a loan and what they will either declare to be a disguised loan or will leave to the trier of fact to determine.

The line between what the courts would recognize or refuse to recognize as a fraudulent device to evade usury as a matter of law and what they would leave to the determination of the trier of fact is a fuzzy one indeed. This ambiguity is evident when one contrasts *Mears v. Mayblum*<sup>17</sup> with *Indian Lake Estates, Inc. v. Special Investments, Inc.*<sup>18</sup> In the first case, Mears sold an interest in land to Mayblum for \$12,000 and simultaneously agreed to purchase it back for \$15,000, repayable without interest within a year, thus affording Mayblum a profit considerably above the lawful interest rate. The supreme court ruled this to be an usurious loan as a matter of law.<sup>19</sup> In *Indian Lake*, a land promoter sold large numbers of land purchase agreements to investors at very substantial discounts. The agreements were highly speculative, and the seller guaranteed their payment. The district court of appeal sustained the chancellor's finding that the transaction was a sale in fact as well as in form, and was not a disguised loan. It quoted, with approval, the following:

The bargain, however, is in terms not a loan but a sale, and though accompanied with a guaranty of the value of the article sold, it should not be regarded as within the purview of statutes against usury, unless the parties are in fact intending a loan rather than a sale; and this is the more general rule.<sup>20</sup>

What objective standard can the trier of fact apply to determine whether the buyer intended a bona fide purchase or a disguised loan where the seller of discounted contracts or notes has been required to endorse them? Since it is legitimate to presume that one intends the necessary consequences of his acts, and since there was no dispute as to facts, other than intent, which had to be inferred, logic dictated in *Indian Lake* that, despite the finding of the chancellor that no corrupt

---

so long as they intend the acts which constitute the giving and receiving of interest in excess of the legal maximum, it is usury.

In this writer's opinion, this is the test which the lender's counsel must apply.

17. 96 So.2d 223 (Fla. 1957).

18. 154 So.2d 883 (Fla. 2d Dist. 1963).

19. This is the exact reverse of a device for evading usury practiced in medieval Europe, known as the "Mohatra." Blaise Pascal, in Letter VIII of "The Provincial Letters," first published in Paris in 1656-57, described the Mohatra as follows: "The Mohatra bargain is effected by the needy person purchasing some goods at a high price and on credit, in order to sell them over again, at the same time and to the same merchant, for ready money and at a cheap rate." For further definition of the Mohatra, see WEBSTER'S INTERNATIONAL DICTIONARY 1578 (2d ed. 1950).

20. 6 S. WILLISTON & G. THOMPSON, WILLISTON ON CONTRACTS § 1689 (rev. ed. 1938) as quoted in 154 So.2d at 889.

intent existed, the district court should have reversed and found usury. In *Mears*, the supreme court, in a factual situation not too different and despite the fact that the chancellor granted a summary decree for the creditor on a finding that no corrupt intent existed, stated: "[T]o consider Mayblum a seller of lands as distinguished from a lender of money requires credulity we do not possess."<sup>21</sup> The decision of the chancellor was reversed and summary judgment was granted for the debtor. In *Holland v. Gross*,<sup>22</sup> the supreme court said:

A finding which rests on conclusions drawn from undisputed evidence, rather than on conflicts in the testimony, does not carry with it the same conclusiveness as a finding resting on probative disputed facts, but is rather in the nature of a legal conclusion.<sup>23</sup>

Hence, it is believed that under the facts of *Indian Lake* the court was presented with a question of law rather than of fact, and that it incorrectly applied the law. To put it another way, whether the contract the parties knowingly entered into is a sale or a loan requires only a legal conclusion.

There is a distinction without a difference to merit it between these two cases. In the latter case, the seller was required to repurchase only if the purchase contracts went into default, whereas in the former, the obligation to repurchase was unconditional. Yet, in *Indian Lake*, it requires "credulity we do not possess" to believe that the parties could have doubted that many of the purchase contracts would not be honored and that the seller would be obligated to repurchase them.

Our only explanation for the decisions in *Indian Lake*, in which the opinion exudes the court's disapproval of the borrower, and in the numerous out-of-state decisions cited therein, most of which involved discounted conditional sales agreements,<sup>24</sup> is that the courts seem to

---

21. *Mears v. Mayblum*, 96 So.2d 223, 225 (Fla. 1957).

22. 89 So.2d 255 (Fla. 1956).

23. *Id.* at 258.

24. *B & D, Inc. v. E-Z Accept. Corp.*, 186 So.2d 29 (Fla. 3d Dist. 1966), also involved the assignment of discounted conditional sales contracts which the seller was required to endorse. The Third District Court of Appeal, after citing *Indian Lake Estates, Inc. v. Special Inv., Inc.*, 154 So.2d 883 (Fla. 2d Dist. 1963), said: "[T]here is sufficient evidence to support a finding by the Chancellor that the transactions involved herein were sales and not loans." *Id.* at 30. Perhaps the second district in *Indian Lake* and the third district in this case felt that although the facts were undisputed, conflicting inferences could be drawn from them, and hence they would not disturb the inferences drawn by the Chancellor who had seen and heard the witnesses. Cf. *Bruce Constr. Corp. v. The State Exch. Bank*, 102 So.2d 288 (Fla. 1958). The rule, therefore, seems to be that where the requirement to repurchase is conditional, even though the facts and circumstances are not in dispute, the Chancellor or other trier of fact is to be permitted, through some unexplained process, to infer the intent of the parties. In *Jones v. Hammock*, 131 Fla. 321, 322, 179 So. 674, 675 (1937), the Florida Supreme Court said:

This court has held that one of the requisites of a usurious transaction is that there must exist a corrupt intent to take more than the legal rate for the use of money loaned . . . and that usury is largely a matter of intent and is not fully determined

bend over backwards to avoid finding the requisite corrupt intent where the means employed is widely followed,<sup>25</sup> where there is no oppression, and where the obligation to repurchase is conditional rather than absolute. After all, the common law is replete with instances where the judges have used illogical excuses to avoid what they considered an unjust or unfair result. The difficulty is that one can never be sure when their sense of fair play will thus assert itself.

While the first question is always whether the transaction is or is not a loan, a second and equally important inquiry is whether the answer depends on a rule of law or a finding of fact.

#### V. THE SALE-LEASEBACK: IS IT A DEVICE TO EVADE USURY OR A LEGITIMATE ALTERNATIVE TO A LOAN?

The sale-leaseback, where A sells a building to B and B leases it back to A for a long period of time, usually on a net lease, is a transaction which has often been entered into where usury is not a factor because the rate of return is well below the limits of usury. The reason for the sale-leaseback's popularity with the financial community is that it generally provides a greater yield than does a mortgage and the rent can be geared to the income of the property or to a price index, thereby providing a hedge against inflation. The latter is a consideration of increasing importance to institutions engaged in long-term financing.

By making a sale and leaseback of his property, the seller-lessee obtains its use, in most cases for the useful life of the improvements, without tying up his assets. He can deduct all the rent as an expense on his federal income tax return. If he had given a mortgage on the property, however, he could only claim interest and depreciation on improvements since land is not a depreciable asset. In some cases where the cost basis exceeds the sale price, it is also possible for the seller to take a capital loss. It is these tax advantages, as well as the freeing of

---

by the fact of whether the lender actually gets more than the law permits, but whether there was a purpose in his mind to get more than legal interest for the use of his money. . . . Also to work a forfeiture under the statute the principal must knowingly or willfully charge or accept more than the amount of interest prohibited.

It seems that whether or not the transaction is a loan calls only for a conclusion of law. If the court decides that it is, the question of fact is then whether there was an intent to extract more than the sum advanced plus interest at the lawful rate. If the evidence showing such a purpose is undisputed and not subject to conflicting inferences, the court should direct a verdict or make a ruling that there is a usurious loan. If there is a conflict or possible conflicting inferences on this point, then the Chancellor's conclusion is one of fact rather than law.

25. The schizophrenic approach which the courts have displayed toward the usury statutes probably reflects, on the one hand, judges' own holy horror at the idea of usury (and of high interest rates generally), and on the other, a vague feeling that the usury laws should not be interpreted so as to interfere with legitimate commercial activities. The result is a hodge-podge with the courts facing first in one direction and then in the other.

Shanks, *supra* note 16, at 343.



capital, which have made the sale-leaseback advantageous and attractive to the seller.<sup>26</sup>

The leaseback, until recently, was almost always for a fixed net rent, but now the net rent is often part fixed and part contingent, which may bring the lessor a yield in excess of the interest limit imposed by the usury statute in loan situations. Where the return on the lease exceeds or may exceed ten percent per annum in the case of an individual or fifteen percent in the case of a corporation, can it be said that this is a disguised loan aimed at evading the usury statute or is it no more than what it purports to be? The answer depends on which of several types of leaseback is employed.

*A. The Sale-Leaseback without Repurchase Agreements,  
Repurchase Options, or Other Frills*

In order to determine whether this type of sale and leaseback can be considered a loan subject to the usury statute, it should first be compared to a ground lease. In an earlier article,<sup>27</sup> this writer pointed out that the long-term ground lease is essentially a security device since the lessor has parted with all of the incidents of ownership except the right to receive rent and a reversion which usually will not come into being until long after the death of the lessor and his children. His only real interest in the property, at least in the earlier years of the term, is in the nature of a lien to secure the rent. The value of the reversion is so small and so speculative that, where the lease still has a long time to run, the Illinois Supreme Court in condemnation proceedings has historically allowed the lessor only the capitalized value of his rent with nothing added for the reversion.<sup>28</sup> The balance of the award goes to the lessee, who is thus treated as the owner of the property. Yet, the ground lease is not considered a mortgage,<sup>29</sup> nor has the usury statute been construed to regulate the rent that can be charged the ground lessee.

26. In *Wilson, Sales and Leasebacks*, 16 U. So. CAL. 1964 TAX INST. 149, there is an explanation of both the economic motives for and the tax results from the sale and leaseback.

27. Anderson, *The Mortgagee Looks at the Ground Lease*, 10 U. FLA. L. REV. 1 (1957).

28. *Chicago & N.W. Ry. v. Chicago Mech. Inst.*, 239 Ill. 197, 87 N.E. 933 (1909); *Chicago W.D. Ry. v. Metropolitan W.S.E.L.R.R.*, 152 Ill. 519, 38 N.E. 736 (1894). In Boyer & Wilcox, *An Economic Appraisal of Leasehold Valuation in Condemnation Proceedings*, 17 U. MIAMI L. REV. 245, 270 (1963), the authors criticize this method of dividing the award between lessor and lessee. There appear to be no Florida cases squarely on point. Despite the arguments of Professors Boyer and Wilcox, it is believed the approach of the Illinois court is a sound one.

29. *Commissioner v. Estate of Simmers*, 231 F.2d 909 (4th Cir. 1956). The ground lease does not meet the definition of a mortgage contained in FLA. STAT. 697.01 (1967):

All conveyances, obligations conditioned or defeasible, bills of sale or other instruments of writing conveying or selling property, either real or personal, for the purpose or with the intention of securing the payment of money, whether such instrument be from the debtor to the creditor or from the debtor to some third person in trust for the creditor, shall be deemed and held mortgages, and shall be subject to the same rules of foreclosure and to the same regulations, restraints and forms as are prescribed in relation to mortgages.

There are similarities as well as differences between a ground lease and a mortgage loan. Both the tenant and the mortgagor are in possession, but the tenant generally receives a different and more advantageous federal tax treatment. Except in the rare case of the lease renewable in perpetuity, possession of the property eventually reverts to the lessor or his heirs, whereas, if the mortgage is satisfied, the mortgagor retains the property.

The resemblance between a ground lease and a leaseback is only superficial. They are similar in that both carry a net rental and customarily run for a long period of time. The typical Florida ground lease is for ninety-nine years, though shorter terms are frequently used. The favored term of the leaseback is the estimated life of the improvements, usually about thirty to forty years. The classic ground lease demises either bare land or land with obsolete improvements which the parties contemplate will be replaced by the lessee. Except where the ground lease contains a subordination clause (or in the few instances where the lessee spends his own money), the cost of the new improvements is financed by a mortgage encumbering only the leasehold. Thus, the ground lessor, once the improvements are erected, looks primarily to them as security for his rent and not to the credit of the ground lessee. Consequently, the unsubordinated ground lease customarily relieves the lessee from liability for breaches of any of the lessee's covenants, including the covenant to pay rent, occurring after assignment, provided that the improvements have been erected.

Almost invariably, the leaseback of the type now being considered demises improved property. The lessor's only assurance that the rent will be paid is the credit standing of the tenant. Hence, the leaseback is nothing but a high-credit net lease, the only distinguishing feature being that in the case of the leaseback the lessor has acquired the property from his lessee rather than from a stranger. There is even less reason for holding it to be a disguised mortgage loan than for holding a ground lease to be a device to evade the usury statute, since the high-credit lease is not a security device by any stretch of the imagination. It is therefore believed that the Florida courts would not hesitate to grant a summary judgment for the lessor should the seller-lessee claim that such a sale-leaseback is a disguised loan.

#### B. *The Sale-Leaseback Where the Seller Must Repurchase*

Where the lessee is required to repurchase the property, at least if the requirement is not conditional, we have precisely the same type of situation which the supreme court declared to be a loan and not a

---

In *Marcus v. Hull*, 142 Fla. 306, 311, 195 So. 170, 172 (1939), the court said: "This court has construed the above statute many times and in effect has held that an instrument *given for the purpose or with the intention of securing the payment of money is a mortgage*. . . ." (emphasis added). It is submitted that neither a ground lease nor a leaseback without an option or contract to repurchase can possibly meet this definition.

sale as a matter of law in *Mears v. Mayblum*.<sup>30</sup> The only question is whether the combined rent and profit on the resale exceeds the maximum lawful rate of interest. As this is mathematically ascertainable, there can be no substantial issue of material fact, at least when the rent is fixed. If the return to the purchaser-lessor exceeds the permissible interest, a summary judgment or directed verdict holding the transaction usurious is to be expected.

The fact that the contract to repurchase is not in the lease, but is contained in a separate but contemporaneous agreement, is immaterial.<sup>31</sup> However, an agreement to repurchase, made subsequent to the sale-leaseback, does not present an issue of fact for the jury since there must be usurious intent at the time the loan is made.<sup>32</sup> Therefore, it is safe for a purchaser-lessor to contract to sell the property back at a profit which, when combined with the rent, will exceed the lawful rate of interest, but only if the resale agreement is made sufficiently subsequent to the sale-leaseback so that it cannot be shown that the contract is part of a scheme hatched when the sale-leaseback was closed. Were the repurchase option granted within a matter of days, there could very well be a jury issue, but a resale agreement entered into months or years later should result in a summary judgment or directed verdict for the purchaser-lessor.

### C. *The Sale-Leaseback with an Option to Repurchase*

Unlike the leaseback where the seller is required to repurchase, the leaseback with only an option to repurchase may or may not be a disguised loan. The controlling factor is the intent of the parties. Thus, in *Helvering v. F & R Lazarus Co.*,<sup>33</sup> a tax case where the outcome depended on whether or not the leaseback which was accompanied by an option to renew and purchase was or was not a disguised mortgage, Mr. Justice Black, speaking for a unanimous court, said:

---

30. 96 So.2d 223 (Fla. 1957).

31. *Connor Air Lines, Inc. v. Aviation Credit Corp.*, 280 F.2d 895 (5th Cir. 1960), *cert. denied*, 364 U.S. 911 (1960); *Marcus v. Hull*, 142 Fla. 306, 195 So. 170 (1939); *Maxwell v. Jacksonville Loan & Imp. Co.*, 45 Fla. 425, 34 So. 255 (1903).

32. The Florida Supreme Court has so ruled many times. *Home Credit Co. v. Brown*, 148 So.2d 257 (Fla. 1962); *Carter v. Leon Loan & Fin. Co.*, 108 Fla. 567, 146 So. 664 (1933). Yet in *Green Ridge Corp. v. South Jersey Mtg. Co.*, 211 So.2d 70, 71 (Fla. 2d Dist. 1968), the court said:

Appellants' first argument is necessarily founded on the theory that the usurious character of a transaction must be determined or determinable at its inception. However, as was pointed out in *Home Credit Co. v. Brown*, Fla. 1962, 148 So.2d 257, modifying Fla. App., 137 So.2d 887, the Florida courts have disregarded such theory. 148 So.2d at 259. The test of usury followed in Florida is not based upon the contingencies inherent in a transaction, but upon what actually develops.

Notwithstanding the above, in *Tel Service Co. v. General Capital Corp.*, 212 So.2d 369 (Fla. 2d Dist. 1968), *rev'd on other grounds*, 227 So.2d 667 (1969), decided only two weeks later, the same court cited its earlier decision in *First Mtg. Corp. v. Stellmon*, 170 So.2d 302 (Fla. 2d Dist. 1964), and said, at 374: "The usurious nature of a contract is to be determined as of the date of its inception."

33. 308 U.S. 252 (1939).

The Board in substantial effect found that the instrument under which the taxpayer purported to convey legal ownership to the trustee bank was in reality given and accepted as no more than security for a loan on the property; the 'rent' stipulated in the concurrently executed ninety-nine year 'lease' back was intended as a promise to pay an agreed five per cent interest on the loan; and the 'depreciation fund' required by the 'lease' was intended as an amortization fund, designed to pay off the loan in forty-eight and one-half years. These findings are supported by evidence which permits, at most, conflicting inferences and are, therefore, conclusive here. And, unless the Board committed error of law we must affirm.

We think the Board justifiably concluded from its findings that the transaction between the taxpayer and the trustee bank, in written form a transfer of ownership with a lease back, was actually a loan secured by the property involved. General recognition has been given the 'established doctrine that a court of equity will treat a deed, absolute in form, as a mortgage, when it is executed as security for a loan of money.' [Citation omitted.] In the field of taxation, administrators of the laws, and the courts, are concerned with substance and realities, and formal written documents are not rigidly binding.<sup>34</sup>

In the usury case of *Kay v. Amendola*,<sup>35</sup> the Second District Court of Appeal upheld a finding of fact that a leaseback with an option to repurchase was a disguised loan. Again, the intent of the parties was the determining factor.

Where the economic realities of the situation dictate, at the time the contract is entered into,<sup>36</sup> that the option will be exercised, it is not too difficult to find the necessary intent. This writer therefore concludes that whether such a leaseback is or is not a disguised loan is essentially a question of fact determinable by a jury, so that counsel for the financial institution cannot advise his client that such a transaction is usury-free except where the combined rent and profit on resale is insufficient to constitute usury or where the option falls into one of the following categories:

1. *An option of first refusal.* It is difficult to see how such an option would put any pressure on the seller-lessee to exercise it. There could be no understanding, implied or otherwise, that the option would be exercised; hence, the second of the four elements of usury<sup>37</sup> would be missing.

---

34. *Id.* at 254.

35. 129 So.2d 170 (Fla. 2d Dist. 1961).

36. See authorities cited at note 32 *supra*.

37. "An understanding between the parties that the money loaned is to be returned." See p. 645 *supra*.

2. *An option to repurchase at the capitalized value of the rent.* As long as the purchase price is fair and the rate at which the rent is capitalized is not out of line, there is again no basis for inferring an understanding that the option will be exercised. Thus, in *Commissioner v. Estate of Simmers*,<sup>38</sup> another federal tax case, A leased land to B under a Maryland ground lease, which was perpetually renewable. The Maryland statute gave B the right to purchase the fee after five years at a price determined by capitalizing the ground rent at six percent. The court said: "While the economic relation between lessor and lessee resembles that of mortgagor and mortgagee, there is the important difference that the purchaser can never be compelled to pay the so-called mortgage debt."<sup>39</sup>

3. *An option at a price to be determined by independent appraisers at a future date.* If the price is the full fair value of the property, again there is no pressure on the seller to exercise the option and no basis for inferring an agreement or understanding that it will be exercised. If the appraisal is contemporaneous with the lease, a jury issue might well be raised if the lessee claimed the appraisal to be a sham. This is the reason for limiting the exception to future appraisals.

#### D. *The Leaseback with a Leasehold Mortgage*

Until quite recently, sales and leasebacks followed the patterns just described. Of late, however, a new type, which for convenience may be called a "mortgaged leaseback," has been developed as a vehicle for equity participation by life insurance companies and similar institutions for financing not the ultimate occupants of the project but rather the developer who builds, leases, and manages it. The transaction is in the nature of a joint venture in which the developer contributes his services and skill but little if any money, and the financial institution contributes all or almost all the money required to purchase the land and erect the improvements. In return for financing the venture, which may be an apartment house, shopping center, industrial park, or other commercial development, the financing institution requires not only that the developer contribute his expertise and services but that he occupy a position subordinate to the institution.

The mortgaged leaseback, which is only one of a number of methods<sup>40</sup> employed for achieving this objective, works as follows: The developer either purchases or obtains an option on a parcel of land. He agrees to sell the fee to the institution, which, in turn, leases the land back to him for a term of thirty to forty years. The purchase price is the value of the land as determined by appraisers selected by the institution. In fixing the value of the land, they presumably do not take into

38. 231 F.2d 909 (4th Cir. 1956). See authorities cited at note 29 *supra*.

39. *Id.* at 915.

40. See Hershman, *supra* note 3.

account the effect of the leaseback on its value. The rent provided in the leaseback is partly fixed and partly a percentage of profits. The total yield is expected to exceed 15 percent per annum on the price paid by the institution for the land. The institution then makes the developer a leasehold mortgage loan amortizable over the maximum possible length of time permitted by the investment statute applicable to it. The interest rate may be fixed or tied to the prime rate but there is a proviso in the note that in no event shall it exceed 10 percent or 15 percent per annum, depending on whether or not the leasehold borrower is a corporation. Any income after the payment of taxes, operating expenses, including a management fee to the developer, and the principal and interest payments on the leasehold mortgage, is divided according to the agreement of the parties, with the institution's share constituting the contingent rent in the leaseback.

By the end of the term, if all goes according to plan, the leasehold mortgage has been repaid, the financial institution has received a high rent under the lease, and it then owns free and clear an obsolescent building on a piece of land which, because of inflation, will probably be worth more than the original price which the institution paid. The developer has pocketed the management fee and his share of the profits during the term of the lease, but upon its termination his interest in the venture ceases.

This is the basic plan of the mortgaged leaseback, but variations are possible. For instance, when the development is in the planning stage, the institution may issue its commitment but not advance any money until the improvements are completed, thereby necessitating construction financing by the developer prior to closing with the permanent investor.

On its face, the mortgaged leaseback is free of usury. It has already been demonstrated that the leaseback which is unaccompanied by a contract of or an option to repurchase is not a loan as a matter of law. The leasehold loan calls for a permissible interest rate. How then can usury exist?

The answer is that it may exist in case the trier of fact finds: (1) That the two transactions are part of a plan involving a corrupt intent to take more for the use of the money loaned on the leasehold mortgage than permitted by the statute; (2) that either the purchase price paid for the fee or the rent exacted is such that it is not an arrangement that would be entered into except to induce the seller-lessee to make the loan;<sup>41</sup> and (3) that the excess over what the institution pays and

---

41. For an example of a tie-in of this type, see *Connor Air Lines, Inc. v. Aviation Credit Corp.*, 280 F.2d 895 (5th cir. 1960). *White v. Ladd*, 155 Fla. 264, 19 So.2d 836 (1944) is a case where a note covered both a loan and compensation for a release. The chancellor's finding of good faith was sustained and the note found not to be usurious. The mere fact that the borrower would not have made the loan but for the simultaneous transaction has been held not conclusive that a bonus was intended. *Bokser v. Lewis*, 383 Pa. 507, 119 A.2d 67 (1956).

what the property subject to the leaseback is worth renders the loan usurious.

If the interest in the leasehold loan is at the maximum permissible rate, any underpayment for the sale-leaseback is additional interest charged the leasehold mortgagor for the use of the money advanced under the leasehold loan and will taint the transaction with usury if the requisite corrupt intent is found.<sup>42</sup> If the interest rate provided in the note is below the limit set by the statute, the borrower can still raise a jury issue if he produces evidence that the excess of true value over price paid, when added to the interest provided on the face of the note, exceeds the permitted rate and the intent was to extract a bonus.<sup>43</sup>

It can therefore be assumed that if the mortgaged leaseback is attacked for usury, it is highly probable that the outcome will turn on an issue of fact, since there can be no doubt that a bonus of this nature will be treated as interest, assuming a corrupt intent is found. Nor will it make any difference if the leasehold lender and the purchaser-lessor are not identical, as when the financial institution makes the mortgage and a subsidiary takes title to the property.<sup>44</sup> If there are completely independent transactions, as where A leases to B and then B obtains his leasehold loan from C, with whom A has no connection, the loan from C would not be rendered usurious just because A drove a hard bargain. In such a case, the only way a jury issue could be raised would be on a claim that A and C were working in tandem.<sup>45</sup>

Where the developer owns the land before the financier enters the picture, and the latter purchases the land and leases it back to his vendor, we have a true sale and leaseback. Suppose, however, the promoter has only an option and the financial institution, upon receiving an assignment of the option, purchases the land from the owner and then leases it to the promoter. Should this make a difference?

---

42. *Mindlin v. Davis*, 74 So.2d 789, 791 (Fla. 1954):

Manifestly, if the transaction presented here, in any of the particulars charged, constitutes a device or contrivance for the exaction of additional interest over that provided in the mortgage note itself, then the whole transaction is rendered usurious inasmuch as ten per cent interest contracted in the note is the maximum allowable under the law.

43. In *Griffin v. Kelly*, 92 So.2d 515 (Fla. 1957), the defendant plead usury in his answer to a complaint seeking enforcement of a note. The answer set out that the defendant, in addition to agreeing to repay the money loaned at six percent per annum interest, was required to and did give the lender an option to purchase stock worth \$59,300 for \$59.30. The lower court gave judgment for the plaintiff on the pleadings, and the defendant appealed. The supreme court reversed, holding that a valid defense had been plead and that the key element was the intent of the parties. It found a bonus of \$59,240.70 had been alleged by the pleadings, and that it would establish usury if proven.

44. In *Connor Air Lines, Inc. v. Aviation Credit Corp.*, 280 F.2d 895 (5th Cir. 1960), the connection between the two corporations was the same president. This was sufficient to enable the court to treat them as one. So, as in *Connor Air Lines*, lenders have repeatedly been found guilty of usury by reason of commissions paid to their agents, brokers, or officers. *Speier v. Monnah Park Block Co.*, 84 So.2d 697 (Fla. 1955); *Richter Jewelry Co. v. Schweinert*, 125 Fla. 199, 169 So. 750 (1936).

45. *Cf. Investment Funds Corp. v. Bomar*, 303 F.2d 592 (5th Cir. 1962), where it was held that a fee to a broker who was not the agent of the lender could not be treated as additional interest.

In *Stark v. Bauer Cooperage Co.*,<sup>46</sup> a Sixth Circuit case, A asked B to purchase land from C and then sell it back to him on credit, which B did at a sufficiently higher price to render the transaction usurious, if the profit could be regarded as interest. The lower court, there being no jury, found the transaction to be a loan; the appellate court reversed and found that the transaction was not a loan. In an almost identical situation, the Supreme Court of Florida reached the opposite conclusion in *Hawley v. Kendall*.<sup>47</sup> It follows that, in Florida, it should make no difference from whom the land is purchased.

In practice, however, this writer believes that it may create a more favorable atmosphere for the financing institution if the purchase is made from a third party. If it is claimed that the terms of the leaseback are unconscionably hard and that it therefore constitutes a premium, it may be easier in such a case for the court to equate the developer, who is also the seller, with the ordinary property owner seeking a mortgage than in the case of the promoter who does not own the land and who only presents to the institution a dream which he hopes to convert into a reality with its money. The purpose of the usury law is to protect the needy borrower.<sup>48</sup> It should not be stretched to impede the promoter seeking risk capital where the capitalist shares in the profits through some means other than a loan.

In *Diversified Enterprises, Inc. v. West*,<sup>49</sup> the plaintiff-appellee had indicated to the defendant a "willingness to invest in a profitable venture." Subsequently, the defendant sought to purchase one tract of land for \$110,000 as downpayment and options on three adjoining parcels for \$10,000 each. The defendant obtained \$10,000 from the plaintiff prior to the day the purchase was to be consummated on only an oral agreement that the money would be returned if the purchase was not closed. As the closing date drew near, the defendant still lacked \$30,000. The plaintiff advanced the additional funds and received in return two \$10,000 notes at ten percent per annum interest and an assignment of one of the three options for which the defendant had paid \$10,000, but the defendant reserved the right to repurchase the option for \$60,000 at any time within one year. The defendant claimed that there were two separate transactions and that the plaintiff received two \$10,000 notes for the initial \$10,000 advanced and the option for the additional \$30,000 advanced at the closing. The plaintiff claimed that the notes were to represent a loan of half of the \$40,000 and that the other half was risk capital, with which he purchased the option. (The defendant had failed to repurchase the option and at the end of the year the plaintiff had sold it to a stranger for \$60,000.)

---

46. 3 F.2d 214 (6th Cir. 1925).

47. 139 Fla. 835, 191 So. 10 (1939).

48. *Stubblefield v. Dunlap*, 148 Fla. 401, 4 So.2d 519 (1941); *Pushee v. Johnson*, 123 Fla. 305, 166 So. 847 (1936); *River Hills, Inc. v. Edwards*, 190 So.2d 415 (Fla. 2d Dist. 1966).

49. 141 So.2d 27 (Fla. 2d Dist. 1962).



In reversing the trial judge and finding the notes untainted with usury, the court said, *inter alia*:

When the principal sum lent or any part of it is placed in hazard, the lender may lawfully require, in return for the risk, as large a sum as may be reasonable, provided it is done in good faith. The risk, however, must be substantial, for a mere colorable hazard will not preclude excessive interest charges from being usurious. . . . In the instant case, plaintiff did not require that more be paid back than was represented by the \$40,000 which defendant received from him; instead there were only the notes representing \$20,000 plus the option for which defendant had paid \$10,000.<sup>50</sup>

Neither this case, nor *Perry v. Beckerman*,<sup>51</sup> which was cited in the opinion, holds that a loan, just because it is speculative, can carry an interest rate in excess of the amount permitted by the usury statute. What both cases recognize is that a transaction may be part loan and part speculation, and that the fact that the two transactions are part of a whole does not render the loan usurious as long as the parties acted in good faith. In neither case did the borrower claim, nor did the facts even indicate, that the granting of the loan was contingent on the borrower's parting with the "piece of the action" represented by the part of the advance treated as something other than a loan of money.<sup>52</sup>

Even in light of the foregoing cases, it is believed that in any case where part of the money is advanced as a loan and simultaneously therewith the lender obtains something else of value by purchase, lease, option, or otherwise from the borrower, a jury issue is a possibility if not a probability and the attorney for the lender should so advise his client.

At this point, it may not be amiss to inquire why the institution bothers with the mortgaged leaseback. Why not make a sale-leaseback without any options or frills, thereby escaping altogether the possibility of usury? The same income can be generated by making the rent part fixed and part contingent.

The reason the life insurance companies, as well as certain other financial institutions, favor the mortgaged leaseback has nothing to do with usury but has much to do with the statutes governing their investments. Leasehold mortgages, if they comply with the requirements of the investment statute, are what are known as "sanctified" investments, that is to say, investments expressly authorized by the statute. Most, if not all, of the states where the bulk of the large life insurance companies are located permit them to own real property for investment purposes (thus sanctifying the investment), but limit such holdings to a small per-

---

50. *Id.* at 30.

51. 97 So.2d 860 (Fla. 1957).

52. This is what distinguishes these cases from *Connor Air Lines, Inc. v. Aviation Credit Corp.*, 280 F.2d 895 (5th Cir. 1960).

centage of their assets. In most states, there is no such limitation on their investments in first mortgages, be they fee or leasehold.<sup>53</sup>

If the institution is investing \$2,500,000 in a non-mortgaged sale and leaseback, the entire sum has to be treated as a real estate holding; on the other hand, if it buys the land for \$250,000 and lends \$2,250,000 on a leasehold mortgage, only \$250,000 is regarded as an investment in real estate. It follows then, that by using the mortgaged leaseback and similar techniques, the life insurance company can increase almost ten-fold the number of developments in which it can take an equity position.

When the \$2,250,000 leasehold loan is to a corporation and the maximum lawful rate is 15 percent per annum, the spread between a hypothetical fixed rate of ten percent per annum on the leasehold loan and 15 percent per annum is so great, even if it were found that the value of the fee with the leaseback were double what the purchaser-lessor paid for it, any bonus resulting from the purchase at \$250,000 could easily be absorbed. This is because 5 percent interest on a loan amortizing monthly over a 30-year period amounts to approximately \$933.20 per \$1,000.00. Thus, in the case of a \$2,250,000 thirty-year loan, there is a spread of over \$2,000,000 between 10 percent and 15 percent interest if the loan runs to maturity. Thus, there is no great risk of usury in most mortgaged leasebacks, and the institution may very well elect to treat the possibility of a jury issue as academic. This is true where the loan is not accelerated in its early years, but suppose a default occurs immediately after the transaction is closed and the leasehold mortgagee wishes to foreclose without delay. In Florida this may pose a real problem.

#### VI. THE FLORIDA RULE ON ACCELERATION AND USURY

Fortunately, this writer is spared the difficult task of analyzing the numerous confusing and conflicting Florida decisions on usury resulting from acceleration, as this has been most ably performed in an article appearing in a recent issue of this publication.<sup>54</sup> The article points out that should prepaid interest, a cash bonus, or "points" be collected in advance and the note accelerated, the period for absorbing such a payment terminates with the entry of a final decree. In such a case, unless the note provides for the return of the unabsorbed interest, the loan is rendered unlawful.<sup>55</sup> A recent case has held that

a transaction which would not have been usurious had it run its full term may become usurious upon acceleration of the balance to early maturity by entry of a final decree. For this to

---

53. FLA. STAT. ch. 625 (1967) is typical. It permits a domestic insurance company to make unlimited investments in fee or leasehold first mortgages meeting the requirements of FLA. STAT. § 625.0126 (1967). It also permits investment in real estate for leasing, FLA. STAT. § 625.0133 (1967), but limits real estate holdings to 10 percent of assets.

54. Boyer & Berger, *Usury and the Viruliferous Acceleration Clause in Florida*, 21 U. MIAMI L. REV. 215 (1966).

55. This is the holding of *First Mtg. Corp. v. Stellmon*, 170 So.2d 302 (Fla. 2d Dist. 1964).

happen, however, acceleration must actually occur or the lender or holder declines [sic] to exercise his acceleration option at the time of his institution of action to enforce the note.<sup>56</sup>

In a case where a cash bonus is collected at the time the loan is closed, it is simple enough to protect the loan from usury by inserting in the note a clause such as this:

In addition to the interest called for herein, makers have paid to payee interest in advance not shown on the face hereof. In the event this note is declared due by the holder prior to maturity and the total amount of interest paid, including interest paid in advance, causes the interest to exceed the rate permitted by law, such interest shall be recalculated and any excess over the interest rate permitted by law shall be credited to principal, it being the intent of the parties hereto that under no circumstances shall the makers hereof be required to pay interest in excess of 15% per annum on outstanding principal balances where the borrower is a corporation or 10% per annum where it is not.

Perhaps, a clause of this nature would protect the mortgaged lease-back from usury, but one cannot be sure when the existence of a bonus depends on a finding that it arose because the investor required that the developer sell him the property and lease it back at an excessive rental. The reason the aforementioned clause is operative to defeat usury in the case of interest or a bonus prepaid in cash is that it shows an intent not to overcharge the borrower. It is self-operating since the excess collected is automatically credited to principal. If the investor contests the claim that it has charged an excessive rental and denies the payment of a bonus, the court might rule that the agreement to return excess interest is not bona fide and only "a device to avoid the penalties of usury,"<sup>57</sup> since it is not intended to become operative unless there is first a finding of a fraudulent intent to exact more interest than is permitted by the statute. Absent any Florida cases on this point, this writer would decline to give an unqualified opinion that such a clause will protect a client where the amount of the bonus is unliquidated and its very existence will be denied.<sup>58</sup> It is therefore believed that in any situation where

---

56. *Green Ridge Corp. v. South Jersey Mtg. Co.*, 211 So.2d 70, 72 (Fla. 2d Dist. 1968). This case was decided after the publication of the article by Boyer & Berger, *supra* note 54.

57. Quoted out of context from the opinion in *First Mtg. Corp. v. Stellmon*, 170 So.2d 302, 310 (Fla. 2d Dist. 1964), where the court said: "Declining to exercise the acceleration option, as we see it, is in the same category as delaying to enforce the obligation. In both instances it may be a device to avoid the penalties attendant upon usury." (Emphasis added.)

58. On June 5, 1970, as this article was submitted for publication, the Florida Legislature amended Florida Statutes section 687.03, by adding the following:

"For the purpose of this section and section 687.02, Florida Statutes, the rate of interest on any loan of money shall be determined and computed upon the assumption that the debt will be paid according to the agreed terms, and in the event said

there is a tie-in between a loan and some other transaction, such as a sale and leaseback or a purchase of stock, to be absolutely safe the institution should utilize one of the methods for avoiding usury suggested in the final sections of this article, at least where the interest rate on the loan is at or near the statutory limit.

## VII. PITFALLS FOR THE UNWARY

It is neither possible nor necessary to review in detail all the techniques used in financing real estate ventures since most techniques are variations of those already discussed. If the borrower is required to sell a portion of its stock or a part ownership of the premises mortgaged to secure the loan, the transaction is basically no different from the mortgaged leaseback. The problem is whether there is a tie-in which will render the loan usurious.<sup>59</sup> Similarly, a loan which calls for a percentage of profits instead of a fixed rate of interest, whatever the rule may be elsewhere,<sup>60</sup> can be usurious in Florida if the return exceeds the lawful rate.<sup>61</sup>

---

loan is paid or collected by court action prior to the term of said loan, any payments charged, reserved, or taken as an advance or forbearance which are in the nature of and taken into account in the calculation of interest, shall be spread over the stated term of the loan for the purpose of determining the rate of interest. "Section 2. This act shall take effect July 1, 1970."

The effect of this amendment is to change the Florida rule on acceleration discussed in this section so that it is now superfluous to insert into the note the clause suggested by the author. Nevertheless, the amended statute is open to several constructions. If the lender makes a 20-year loan to an individual at  $8\frac{1}{2}\%$  interest with a 4-point bonus, it clearly cannot be usurious since the 4 points would be spread over the 20-year term for determining the rate if acceleration took place. However, if the mortgage is foreclosed at the end of one year, could the lender retain the points or would he have to return the "unearned" interest? If he has to return unearned interest, is he allowed to compute earned interest at 10% per annum or must he compute it at 8.7% ( $8\frac{1}{4}\%$  fixed interest plus  $\frac{1}{20}\%$ , which is  $\frac{1}{20}$  of 4 points)? This author's belief is that the courts will not permit the lender to retain unearned interest and that they will calculate earned interest in the way most favorable to the borrower.

Furthermore, this article expressed doubt that the insertion of the suggested clause in a note would be effective in the case of a mortgaged leaseback where the court found that there had been a bonus in the form of underpayment for the fee, because the court might find that where the lender denied the existence of the bonus, the insertion of the agreement to refund interest was not made in good faith. It is believed that the statute removes this doubt since it, and not the contract, establishes the formula, and in case the court should now find that a bonus in fact was paid, it would be spread over the stated term of the loan to determine whether or not usury is present, although the borrower would probably receive credit in the foreclosure decree for unearned interest. Despite its ambiguity, the amendment could prove a real boon to financial institutions which combine ownership of the fee with ownership of the leasehold mortgage.

59. This was precisely the situation in *Connor Air Lines, Inc., v. Aviation Credit Corp.*, 280 F.2d 895 (5th Cir. 1960).

60. It seems to be substantially the same as in Florida. See *Hershman, supra* note 3, at 316.

61. The wording of FLA. STAT. § 687.03 (1967) makes this conclusion inevitable. In *Beach v. Kirk*, 138 Fla. 80, 84, 189 So. 263, 268 (1939), the court said:

We are also ready to agree with plaintiff's counsel when they say that a loan is free from usury where, in lieu of interest, a share of the profits expected to be realized by the borrower is agreed bona fide to be given to the lender as compen-

It is important, however, that we consider certain items, frequently overlooked by lenders, which our courts may hold to be interest. Two are of particular importance: the standby fee and the commission to the loan broker. As far as this writer can discover, there are no Florida cases on the standby fee.<sup>62</sup> Home office counsel will argue that this is not interest, but a sale of credit.<sup>63</sup> Be that as it may, the standby fee can be used as a vehicle for extracting usury,<sup>64</sup> and where a loan is at the maximum lawful rate it is not good judgment to risk the forfeitures imposed by the usury statute for the sake of the few dollars involved in most standby fees. In such a case, the lender should agree to return the fee if and when the loan is closed.

Most, but not all, insurance companies employ loan correspondents who solicit loans in their behalf and service them after closing. The correspondents do not issue loan commitments but send the applications to the insurance companies, who either accept or reject them. It is common practice for loan correspondents to collect a fee from the borrower, as well as from the lender. Such fees to an officer or agent of the lender,<sup>65</sup> or to its broker,<sup>66</sup> as distinguished from a broker acting for the borrower,<sup>67</sup> have been held to be interest and can convert an otherwise lawful loan into an usurious one. The lender should demand a complete disclosure of fees paid to its correspondent. The closing attorney, in case

---

sation for the loan. *Johnston v. Ferris*, 14 Daly (N.Y.) 302; *Goodrich v. Rogers*, 101 Ill. 523. *But it is also true that a stipulation for a share of the profits in addition to the principal and legal interest is usurious.* *Sweet v. Spence*, 35 Barb. (N.Y.) 44 (emphasis added).

When one accepts a percentage of profits instead of fixed interest, the test seems to be whether the parties could expect a return greater than the interest allowed by law or whether the return is truly uncertain. In *Beach v. Kirk*, the court quoted the following from *Colton v. Dunham*, 2 Paige (N.Y. 267) 269: "A contingency merely nominal, with little or no hazard to the principal of the money loaned or advanced cannot alter the legal effect of the transaction." See also, *Diversified Enterprises, Inc. v. West*, 141 So.2d 27 (Fla. 2d Dist. 1962). None of these cases covers the situation where only the return is speculative.

The conclusion is that a loan with a substantial fixed interest plus a contingent interest, which together bring a return greater than permitted by the statute, is almost certain to be usurious, but that if it is wholly contingent and speculative it may not be. In either event, however, the trier of fact would be required to determine intent. See *Stewart v. Nangle*, 103 So.2d 649 (Fla. 2d Dist. 1958). Therefore, counsel for the lender cannot give an opinion that such a transaction is free of usury.

62. The standby fee is a charge which the lender exacts for agreeing to lend money in the future. The lender usually keeps it, whether or not the borrower elects to go through with the loan. For a discussion of charges which can be passed to the borrower, see Comment, *Evasion and Avoidance of Florida Usury Laws*, 5 MIAMI L. Q. 493, 499 (1951).

63. Shanks, *supra* note 16, at 336, concludes: "The fee is for the promise to lend money in the future, not for the loan of the money itself."

64. There may be a jury question as to whether the parties intended that this fee be a device to enable the lender to obtain more than the permitted interest.

65. *Richter Jewelry Co. v. Schweinert*, 125 Fla. 199, 169 So. 750 (Fla. 1936); *Enstrom v. Dunning*, 124 Fla. 571, 169 So. 385 (1936); *Pushee v. Johnson*, 123 Fla. 305, 166 So. 847 (1936).

66. *Speier v. Monnah Park Block Co.*, 84 So.2d 697 (Fla. 1955).

67. *Investment Funds Corp. v. Bomar*, 303 F.2d 592 (5th Cir. 1962); *Graham v. Fitts*, 53 Fla. 1046, 43 So. 512 (1907); *Shaffran v. Holness*, 102 So.2d 35 (Fla. 2d Dist. 1958).

the interest rate is at or near the maximum, should verify all sums paid to the correspondent.

A third danger arises out of a common practice—the purchase of the note and mortgage from the construction lender. This practice arose at the insistence of the borrower when interest rates were still under six percent per annum. If the permanent lender would purchase the note and mortgage from the construction lender, it saved the borrower from paying a new set of intangible and stamp taxes, which together amount to \$3.50 per thousand dollars borrowed. Recently, the construction lender has used this practice as a means for obtaining a greater interest rate than would otherwise be permissible. He may, for example, make a loan at nine percent per annum interest and collect a bonus of three percent. If the loan were only for a year and the borrower were an individual,<sup>68</sup> this would be usurious. However, if he makes the note for the period of both the construction loan and the permanent loan, the bonus can easily be absorbed within a few months or years after the loan is assigned to the permanent lender. Often, the permanent lender is not informed of this bonus, but any loan broker, attorney, or insurance company officer who does not suspect the bonus is lacking in sophistication. The Florida statute<sup>69</sup> provides that a bona fide endorsee or transferee of negotiable paper before maturity, without actual notice of usury, is protected when notice does not appear on the face of the paper. This is a slender reed upon which to lean for two reasons: Frequently, the note does not meet the tests of negotiability;<sup>70</sup> even when it does, the borrower, at some future date, can raise a jury issue by swearing that the attorney or the loan correspondent, both of whom are agents of the lender, had knowledge of the bonus. The safe procedure is to obtain affidavits or estoppel letters from both the borrower and the construction lender when the paper is assigned to the permanent lender. When the attorney representing the permanent lender draws the original loan documents for the construction lender or examines them prior to any funds being advanced, he should insist upon a return of excess interest clause, such as the one heretofore quoted.<sup>71</sup> Then at the closing, assuming his client is willing to purchase the paper under the circumstances,<sup>72</sup> he

---

68. Even if the borrower were a corporation, this may be usurious when the construction loan is advanced in installments, as is invariably the case. The actual effective rate can exceed 15 percent per annum on funds from time to time outstanding.

69. FLA. STAT. § 687.04 (1967).

70. The requirements for negotiability are set out in FLA. STAT. § 673.3-104 (1967).

71. See p. 659 *supra*.

72. The permanent lender is usually neither interested in, nor connected with, the construction lender and sometimes will refuse to purchase the paper if points have been charged, despite an agreement of reimbursement. The author believes this position is not warranted where the construction lender is a bank or other responsible institution. In today's tight-money market, construction money is not available except at a very high premium. If the permanent lender refuses to cooperate, the Florida construction lender can obtain only 10 percent per annum interest from an individual or 15 percent from a corporation. The only way the developer can then do business is to go to a bank in a state, such as Massa-

should obtain an agreement from the construction lender to reimburse the permanent lender if it has to refund any part of the bonus because of this provision.

A common practice of banks is to require that borrowers maintain so-called "compensating balances" as a condition to obtaining a loan. Thus, they may lend an individual \$100,000 at ten percent interest, but require him to maintain a checking account balance of \$20,000 with them. There are Florida cases<sup>73</sup> where the facts are almost identical and usury has been found. While the possibility of usury in such cases is a greater threat to banks making the construction loan than to insurance companies or other permanent lenders, they should nevertheless be alert to this possibility when they purchase mortgages from construction lenders.

Since the construction lender customarily endorses without recourse, the purchaser of the note should require some indemnification against undisclosed usury.<sup>74</sup> A written representation by the borrower that the note is free of usury, given as an inducement to the permanent lender to purchase the note rather than to make a new loan, would probably be effective to estop him should he later assert usury.<sup>75</sup>

#### VIII. METHODS OF AVOIDING USURY

There are three recognized and lawful methods for avoiding usury in Florida. If it appears the interest rate may exceed ten percent per annum but will definitely be less than 15 percent per annum, the lender may insist that the borrower either incorporate or transfer the property to an existing corporation, which will then borrow the money. A second method, which will totally exempt the transaction from the operation of the usury statute, is to secure the loan by a mortgage bond rather than by a note and mortgage. The third method is to subject the transaction to the law of a foreign jurisdiction which either has no usury statute, which exempts loans of over a certain figure, or which denies to corporate borrowers the defense of usury and holds that as a matter of law it is avoidance and not evasion to require a borrower to incorporate as a condition for making the loan. Let us examine each of these means.

---

chusetts, where there is no limit on what the bank may charge. This is simply not possible in most cases, and this attitude by the permanent lender, if adhered to, can prevent the development from materializing.

73. Cf. *American Accept. Corp. v. Schoenthaler*, 391 F.2d 64 (5th Cir. 1968); *Mindlin v. Davis*, 74 So.2d 789 (Fla. 1954); *Williamson v. Clark*, 120 So.2d 637 (Fla. 2d Dist. 1960). There are cases completely on all fours in other jurisdictions holding this a usurious device. *Planters' Nat'l Bank v. Wysong & Miles Co.*, 177 N.C. 380, 99 S.E. 199 (1919); see *Annot.*, 12 A.L.R. 1422 (1921); *East River Bank v. Hoyt*, 32 N.Y. 119 (1865).

74. He may have it anyway by virtue of FLA. STAT. § 673.3-417 (1967), but to require an express indemnification agreement should discourage a construction lender from knowingly trying to unload a note tainted with usury.

75. *Enstrom v. Dunning*, 124 Fla. 571, 169 So. 385 (1936).

### A. *Requiring the Borrower to Incorporate: Avoidance not Evasion*

Formerly, the Florida usury statute declared all loans with interest in excess of ten percent per annum usurious, but corporations were denied the defense of usury.<sup>76</sup> The present statute<sup>77</sup> declares that loans to corporations where interest is in excess of 15 percent per annum are usurious and permits corporations to plead usury. It condemns "any contract, contrivance or device whatsoever" used to extract from the debtor a greater rate of interest than permitted. Requiring the borrower to incorporate, while it no longer eliminates the defense of usury, still gives the lender the benefit of the greater rate, which, in many cases, may prevent any possibility of usury.

It would not seem very difficult to tell whether a loan is to a corporation or to an individual, but from time to time individuals have asserted that the creditor has used the "device" of a corporation to obtain an annual rate of interest in excess of ten percent where the loan is in reality to an individual. New York has taken the position that requiring a loan applicant to form a corporation and then making the loan to it is a lawful avoidance;<sup>78</sup> New Jersey, on the other hand, has held that whether it is avoidance or evasion depends on intent.<sup>79</sup> It is a rule of law in New York but raises a question to be decided by the trier of fact in New Jersey.

The first important Florida case on this subject, which was decided by our supreme court in 1956, is *Holland v. Gross*.<sup>80</sup> In that case, the plaintiff-borrower sought to have the debt declared invalid because of usury. The plaintiff's claim of usury was predicated upon the contention that the loan was actually made to him as an individual and not to the corporate maker, and that the use of the corporation was a device to evade the usury limit. It is not clear whether the corporation was already in existence or whether it was formed solely for the purpose of executing the loan documents. In any event, the master found that the loan was to the corporation, and that the evidence did not support the claim that the loan was to the individual even though he was the corporation's sole stockholder.

The actual holding of the supreme court was that it will not disturb a master's findings of fact unless: (1) there is no substantial evidence to support it, (2) it is clearly against the weight of the evidence, or (3)

---

76. Fla. Laws 1955, ch. 29705, § 20.

77. FLA. STAT. § 687.03 (1967).

78. *Jenkins v. Moyse*, 254 N.Y. 319, 172 N.E. 521 (1930); see Annot., 74 A.L.R. 205 (1931); *Hoffman v. Lee Nashem Motors, Inc.*, 20 N.Y.2d 513, 231 N.E.2d 765, 285 N.Y.S.2d 68 (1967); *Leader v. Dinkler Mgmt. Corp.*, 20 N.Y.2d 393, 230 N.E.2d 120, 283 N.Y.S.2d 281 (1967). Maryland has taken the same position as New York. *Rabinowich v. Eliasberg*, 159 Md. 655, 152 A. 437 (1930).

79. *In re Greenberg*, 21 N.J. 213, 121 A.2d 520 (1956) (an attorney was disciplined for forming a corporation for the borrower so the lender could charge excessive interest); *Gelber v. Kugel's Tavern, Inc.*, 10 N.J. 191, 89 A.2d 654 (1952).

80. 89 So.2d 255 (Fla. 1956).



it was induced by an erroneous view of the law. In any event, the court quoted, with approval, the following:

[T]he fact that a corporation was organized for the sole purpose of taking the loan and escaping the usury laws will not enable it to interpose the defense of usury in the face of such a statute. If, on the other hand, a loan is actually made to an individual, although in form to a corporation, the usury defense may be raised to defeat the obligation. The mere fact that the sole owner of the corporate stock is an individual is alone not enough to indicate that the loan was made to the individual so as to make available to the corporation the usury defense. . . .<sup>81</sup>

The court further stated that:

While the corporate entity may generally be disregarded where it is used as a cloak or cover for fraud or illegality, the corporate entity of a corporation organized merely for the purpose of executing a mortgage on terms usurious in the case of an individual may not be disregarded in order to let in the defense of usury, available to an individual, but not to the corporation. . . .<sup>82</sup>

Subsequently, the various district courts of appeal were confronted with a number of cases where loans to corporations were alleged to be loans to individuals. The first of these was *Gilbert v. Doris R. Corp.*<sup>83</sup> In this case, Valois sought to obtain a loan from Gilbert. Gilbert, in order to obtain more than ten percent interest, required him to form a corporation. The chancellor found that this was the only purpose of the corporation, that it was a device to evade the usury law, and that the loan was actually made to the individual. There is no indication in the opinion that there was any evidence that the money was not paid to the corporation to which Valois conveyed the property which the lender sought to foreclose.

The court concluded there was sufficient credible evidence to support the chancellor's findings of fact, though it saw no useful purpose in reviewing the evidence.

Whether a loan to a corporation is a device to avoid the usury law as being one which is actually a loan to an individual, or whether the corporation is a real and genuine borrower at the higher (15%) rate, as authorized under the usury law, is a question of fact to be determined in each case.<sup>84</sup>

This case seems to hold that the mere fact that the corporation was formed solely to avoid the usury limitation of ten percent per annum

---

81. Quoted from 91 C.J.S. *Usury* § 74 (1955).

82. Quoted from 55 AM. JUR. *Usury* § 105 (1946).

83. 111 So.2d 682 (Fla. 3d Dist. 1959).

84. *Id.* at 685.

interest to individuals supports a finding that the loan was to the individual, not to the corporation. This conclusion, however, may be doubtful because the court did not review the evidence.

The next important case is *Rosenhouse v. Kimbrig*.<sup>85</sup> In *Rosenhouse*, the corporation which borrowed the money was already in existence and already owned the property which it mortgaged. The purpose of the mortgage was to refinance an existing corporate mortgage. The fact that four days later the corporation conveyed the property to the individuals who had endorsed the note was not evidence that the lender had "expected" or "known" that this would take place. The summary decree in favor of the lender was sustained. This decision implies that if the lender knew of the intention to transfer the property to the endorsers before the loan was made, a jury issue would have been raised.

*Rosenhouse* was followed by *Atlas Subsidiaries of Florida, Inc. v. O. & O. Inc.*<sup>86</sup> The final decree in the lower court provided:

[T]he court finds that it has been proved by a preponderance of evidence that the defendants Atlas Subsidiaries of Florida, Inc., a Florida corporation, and Atlas Credit Corporation, a foreign corporation, on September 4, 1962 made a loan of \$11,000 which, while ostensibly and in form a loan to the plaintiff corporation O. & O. Inc., was actually made to the individual plaintiffs, Joseph D. Osterhuber and Mae Osterhuber, his wife. That loan was evidenced by a mortgage note for the face amount of \$16,800 with annual interest thereon at the rate of six per cent. The individual plaintiffs were required by the defendants as a condition of making the loan to guarantee the payment of the mortgage note, which they did by endorsement in writing. That corporation was formed and incorporated under the laws of Florida, at the insistence of the defendant and as a prerequisite to their making of the loan, as a sham contrivance or device, for the purpose of evading the provisions of Chapter 687 of the Florida Statutes by charging and collecting a rate of interest greater than ten per cent per annum. . . .<sup>87</sup>

The appellate court found there was ample evidence to support the finding of the chancellor.

The difference between this case and *Gilbert v. Doris R. Corp.*<sup>88</sup> is that the lender not only required the formation of the corporation, but it also required the individual to endorse the note. The requirement of endorsement was an added fact supporting the contention that the loan was really to the individual. However, it is probable that this decision would not be followed today,<sup>89</sup> since under Florida Statutes section

---

85. 147 So.2d 354 (Fla. 2d Dist. 1962).

86. 166 So.2d 458 (Fla. 1st Dist. 1964).

87. *Id.* at 459.

88. 111 So.2d 682 (Fla. 3d Dist. 1959).

89. It was not followed in *Tel Service Co. v. General Capital Corp.*, 227 So.2d 667

687.11 the liability for interest of an individual secondarily liable for a corporate obligation is limited to ten percent per annum. The statute provides that only the excess over that amount, if claimed against the individual, shall be forfeited. Hence, it is not necessary to state in the endorsement or guarantee agreement that the individual endorsers or guarantors do not guarantee annual interest beyond the permissible figure of ten percent. This case illustrates the necessity of examining the usury statute being construed before evaluating the effect of a decision on the existing statute.<sup>90</sup>

The latest Florida case is *Tel Service Co. v. General Capital Corp.*<sup>91</sup> The trial court found that the lender required the borrower to change its form from a partnership to a corporation so as to enable it to charge more than ten percent annual interest. The supreme court held that "such testimony without more is insufficient to form the basis for disregarding the corporate entity" and reversed the finding of the lower court that the loan was made to the individuals. The court said:

In reaching the conclusion that the present case is governed by the principle enunciated in *Holland v. Gross*, supra, we did not overlook cases cited by Appellants where corporate entities were disregarded because of findings by trial courts that loans were in fact made to individuals and that the corporations formed were devices to evade the usury laws. See *Gilbert v. Doris R. Corporation*. . . . We believe the principles adhered to in the cases just cited are entirely consistent with the rule announced in *Holland v. Gross*, the distinguishing feature being only in the application of the principles to the facts presented in each case.

The testimony offered by Grass to the effect General Capital insisted on the formation of a corporation to be the borrower in order that a higher rate of interest could be charged when the loans were made is not sufficient to establish the loans were actually made to Grass and Noll. Such testimony, without more, is insufficient to form the basis for disregarding the corporation entity. We conclude, therefore, that on the record before us the trial court erroneously found that the loan transactions were made to the individuals, Grass and Noll, rather than to the Appellant corporation, Tel Service.<sup>92</sup>

This writer does not construe this case to approve the decision in *Gilbert v. Doris R. Corp.*, but merely to affirm the pronouncement con-

---

(Fla. 1969). However, the court did not discuss the fact that the owners of the corporation had endorsed the note.

90. The Florida courts have pointed out, from time to time, that the Florida statute is unique; hence, out-of-state decisions are of doubtful authority. *Maxwell v. Jacksonville Loan & Imp. Co.*, 45 Fla. 425, 34 So. 255 (1903); *Enstrom v. Dunning*, 124 Fla. 571, 169 So. 385 (1936).

91. 227 So.2d 667 (Fla. 1969).

92. 227 So.2d at 670.

tained therein that a loan which is in fact made to an individual may be usurious even though the corporate shell is used. *Tel Service Co. v. General Capital Corp.* says unequivocally that requiring the formation of a corporation in order to charge the higher interest rate is not, standing alone, enough to warrant a finding that the loan to the corporation is in fact a loan to the individual. This is a rule of law, not a finding of fact. Were it otherwise, no Florida attorney could give an opinion that any loan to a newly formed corporation where interest exceeds ten percent per annum is free of usury. Now, such an opinion can be given unless there is evidence to show the loan was not to the corporation; and the fact that the lender required the borrower to form the corporation, without more, will not support a finding that the loan is to the individual rather than the corporation.

From the above cases, certain definite conclusions may be drawn: 1) In Florida, it is permissible as a matter of law to require a partnership or individual to incorporate in order to charge the greater interest allowed on loans to corporations. This is not an evasion but a lawful avoidance. 2) The loan is not rendered usurious because the corporation subsequently conveys to an individual, provided the lender had no knowledge of such an intent at the time he made the loan. Nevertheless, a jury issue might be raised if the borrower claims the lender had such knowledge. Therefore, a prudent lender should provide in the mortgage that the corporate borrower may not be dissolved nor may the property be conveyed to its stockholders without the lender's consent. The lender should be very wary about giving such consent in the early stages of the loan. 3) The lender should be careful to pay the proceeds of the loan to the corporation, not to its stockholders. The lender jeopardizes its position by ignoring the corporate entity. 4) In spite of *Atlas Subsidiaries of Florida, Inc. v. O. & O., Inc.*,<sup>93</sup> this writer does not think that requiring the owner of the corporation to endorse would now justify a court in holding the loan was to the individual, since his liability for interest has been limited by statute to ten percent per annum. However, until the point is adjudicated,<sup>94</sup> it may be the path of caution to avoid this requirement in the case of a newly formed corporation. Where, as in *Rosenhouse v. Kimbrig*,<sup>95</sup> the corporation is already in existence and already owns the property to be mortgaged, it is considered safe to require an endorsement or guarantee.

### B. Use of Mortgage Bonds

Florida Statutes section 687.03, which defines unlawful rates of interest, contains the following limitation: "The provisions of this sec-

---

93. 166 So.2d 458 (Fla. 1st Dist. 1964); see note 87 *supra* and accompanying text.

94. *Tel Service Co. v. General Capital Corp.* has probably settled the point, but since the court did not discuss this question in its opinion, the author is reluctant to rely on it as authority for the proposition.

95. 147 So.2d 354 (Fla. 2d Dist. 1962); see note 85 *supra* and accompanying text.

tion shall not apply to sales of bonds in excess of one hundred dollars and mortgages securing the same, or money loaned on bonds."

No cases construing this provision have been discovered, but in view of the Florida Supreme Court's ruling in *Tel Service Co.* that it is not an evasion for the lender to require that the borrower incorporate for the sole purpose of permitting the lender to charge the greater rate of interest, it is clear that requiring first mortgage bonds instead of the more customary<sup>96</sup> mortgage and note would be held a lawful means of removing the transaction from the operation of the statute. It is therefore permissible for the lender to charge any amount he can induce the borrower to pay if the loan is evidenced by a bond or bonds.<sup>97</sup>

### C. Contracting for the Law of Another Jurisdiction

This method, whose leading proponent is Hershel Shanks<sup>98</sup> of the District of Columbia Bar, finds support in several Florida cases,<sup>99</sup> which hold that where there is no agreement between the parties that Florida law shall apply, the applicable usury statute is that of the jurisdiction where payment is to be made, subject, however, to the qualification that there must be some reasonable contact with the state selected as the locale for payment.<sup>100</sup>

Where the original payee of the mortgage note is a New York corporation and the maker a Florida corporation, the note can be made payable in New York. Provided the parties really intend that payment be made in New York, its law will apply even though the note is executed and delivered in Florida and secured by a mortgage on Florida real estate. Since New York denies the defense of usury to corporations except where the rate exceeds 25 percent per annum and recognizes that it is not an evasion to require incorporation solely to prevent usury, the lender is able to charge up to 25 percent per annum with impunity. If the lender actually requires payment of loan installments in Florida,

96. Out of approximately three hundred Florida commercial mortgages handled by this writer, only one has been evidenced by a corporate bond instead of by a note.

97. It is beyond the scope of this article to discuss the technical requirements of a bond or to attempt to distinguish a bond from a note. These requirements and distinctions are uncertain, which is probably the reason this method of usury avoidance has been neglected.

98. See Shanks, *supra* note 16, at 350.

99. *American Clearing Co. v. Walkill Stock Farms Co.*, 293 F. 58 (S.D. Fla. 1923); *Porter Interests v. Missouri State Life Ins. Co.*, 105 Fla. 550, 141 So. 741 (1932); *Thompson v. Kyle*, 39 Fla. 582, 23 So. 12 (1897). Although these cases each apply the law of the place of payment, it is believed that the Florida Supreme Court would today apply the rule quoted at note 101 *infra*. While Judge Tuttle in *Fahs v. Martin*, 224 F.2d 387 (5th Cir. 1955) thought *Thompson v. Kyle*, 39 Fla. 582, 23 So. 12 (1897), was in conflict with this rule, it is believed that it can be distinguished, because the contacts were overwhelmingly in Alabama, where the note was payable. The note was executed there, made payable there, and the parties resided there. Only the security was in Florida. In footnote 9 to *Fahs v. Martin*, Judge Tuttle said "we decide only that Florida would now follow the generally accepted rule of conflicts relating to usury." Cf. *Atlas Subsidiaries, Inc. v. O. & O., Inc.*, 116 So.2d 458 (Fla. 1st Dist. 1964).

100. *United Drivers Supply Co. v. Commercial Credit Co.*, 289 F. 316 (5th Cir. 1923); *Atlas Subsidiaries, Inc. v. O. & O., Inc.*, 166 So.2d 458 (Fla. 1st Dist. 1964).

however, as would most insurance companies, a mere recitation in the note that it is payable in New York is likely to be treated as a sham. Perhaps, if the negotiations for the loan and the closing took place in New York, the courts might be willing to overlook the fact that payment is required in Florida, at least if the note stipulated that New York law is to apply.<sup>101</sup>

But what if a loan from a Florida bank or insurance company is closed in Miami, but made payable in Atlanta? Georgia exempts loans of over \$100,000 from its usury statute.<sup>102</sup> This would be regarded as an attempted evasion of the Florida statute unless there were some bona fide reason, other than the desire to take advantage of Georgia's liberality, for requiring payment to be made there. Additional Georgia contacts would be imperative.<sup>103</sup>

The incorporated loan correspondent for one of the Massachusetts life insurance companies doing business in Florida maintains its home office in Atlanta, with only a branch office in Florida, from which it solicits Florida loans. All servicing of loans comes from the Atlanta office, and payment records are fed into the correspondent's computer there. Perhaps, this might warrant the application of Georgia law rather than that of either Florida or Massachusetts, assuming that the note were made payable in Atlanta. It would certainly be desirable in such case to have the note specify that Georgia law is to apply. The lender's position would be further strengthened if the closing took place in Atlanta and funds were disbursed there.<sup>104</sup>

Where the lender is a Florida bank or insurance company, we do not advocate attempting to contract for the law of another jurisdiction even if the closing is held there. Under such circumstances, the transaction is too difficult to justify, although if two Florida residents are in another state and one lends money to the other while there, and the loan is payable there, we believe the foreign law would apply though the loan is secured by a mortgage on Florida real estate.

---

101. *Fahs v. Martin*, 224 F.2d 387 (5th Cir. 1955), where the court stated:

But with respect to the question of usury, it may be stated as a well-established rule that a provision in a contract for the payment of interest will be held valid in most states if it is permitted by the law of the place of contracting, the place of performance, or any other place with which the contract has any substantial connection. (emphasis supplied). *Id.* at 397.

102. A list of recent changes in the usury statutes of the different states is contained in the appendix. This list was prepared by Lon Worth Crow Company of Miami, Florida, and is reprinted with its permission.

103. See *Atlas Subsidiaries, Inc. v. O. & O., Inc.*, 166 So.2d 458 (Fla. 1st Dist. 1964).

104. The courts have given weight to contract provisions stating which law is to apply if there are sufficient contacts in the state whose law the parties select. *But see* cases discussed in *Whitman v. Green*, 289 F.2d 566 (9th Cir. 1961). Idaho law holds that a mortgage loan by a foreign corporation doing business in Idaho is governed by Idaho law, where the mortgage and note are executed in that state, even though made payable at the lender's out-of-state home office. This is not the general rule. Nevertheless, in *Whitman*, where the closing took place out of state, the court applied the law of the place where the note was delivered and made payable, which was also the domicile of the lender, rather than the law of Idaho.

There are practical difficulties which will have to be overcome, before the avoidance of usury by contracting for foreign law can be widely utilized.

Most Florida developers get their construction money through Florida banks. These banks are not interested in making construction loans unless they can get points which will enable them to earn a very high rate, frequently in excess of 15 percent per annum, on their outstanding loan balances. We have already pointed out that the only way they can do this without violating the usury statute is to collect points and make the note run for the period of both the construction and the permanent loan, while keeping the rate specified in the note at less than the permissible maximum to absorb the points over the stated term of the loan. The construction lender insists upon a take-out agreement with the permanent lender whereby it obligates itself to purchase the paper when construction is completed. Except where out-of-state banks participate in the loan, it is extremely difficult, if not altogether impossible, to effectively contract for the application of foreign law. However, in most large construction loans, foreign banks do participate. There is no valid reason why such loans have to name the local bank as the payee. If the note and mortgage run to the foreign bank and disbursements are made by it after the local bank has approved the advance, it is believed that the note could be made payable in the home state of the foreign bank and its law would then be applicable, especially if the note so stipulates. The fact that the note and mortgage are later assigned to an insurance company which collects its installment payments in Florida should be immaterial since the election to apply foreign law was justifiable when the note was executed. Where this method is employed, extreme care should be exercised to be sure that the local bank does not collect interest, make disbursements, or otherwise treat the fact that the payee is the foreign bank as a fiction. If it does, the courts will probably follow its lead. Therefore, the permanent lender should require some sort of warranty that the note is governed by foreign law.

In cases where the original loan runs to the insurance company, for example, when it makes the construction as well as the permanent loan, the problem is administrative rather than legal. The company's collection procedures would have to be changed before it could effectively utilize the law of its home state. Almost invariably, the servicing records are kept in Florida. It would not seem at all practical to have the payments made at the home office unless the records were kept there. In any event, this is a decision for the home office, not for local counsel.

## IX. CONCLUSION

As a practical matter, most of the new techniques for financing Florida real estate pose few real, as opposed to theoretical, threats of usury where the developer is a corporation. Since October 30, 1969, when

*Tel Service Co.* was decided by the Florida Supreme Court, it has been abundantly clear that a lender can safely insist that the borrower incorporate, and this is generally done in the case of most large developments. Occasionally, however, there may be a possibility that the interest rate could exceed 15 percent per annum, and the lender may not wish to limit itself to that rate. In such a case, a bond issue would appear to afford complete protection to the lender. However, the fact that the provision of the Statute exempting bonds from usury has never been judicially interpreted poses problems for Florida lawyers.

If, for tax or other reasons, the borrower cannot afford to incorporate, an alternative route—contracting for the law of a foreign jurisdiction—is open to the out-of-state institutional lender, provided that certain practical problems can be overcome.

The fact that the permanent lender is an out-of-state institution, however, is no guarantee that this method of usury avoidance can or will be utilized in all cases.

In our opinion, the Florida usury statute should be overhauled and loans for the development of substantial commercial real estate ventures should be exempted entirely from its operation, as has recently been accomplished elsewhere.<sup>105</sup> In the meantime, however, it is not too difficult for institutional lenders to find lucrative opportunities in Florida for financing real property in a way that does not conflict with our present usury statute.

---

105. See APPENDIX *infra*.



*APPENDIX\**

*Compilation  
of  
Mortgage Bankers'  
Answers  
to  
Interest Limitation Survey*

Questionnaire and Compilation Prepared by:  
LON WORTH CROW COMPANY\*\*

---

\* The attached survey is not intended to be a legal digest of usury statutes. The questionnaires were forwarded to Mortgage Bankers "in the field" and represent their understanding of the interest limitations under which they operate.

\*\* Mortgage Bankers, Miami, Florida.

## APPENDIX (continued)

State	Individual	Corporate	Other (Partnership, Trust, Etc.)	Exemptions from Usury Limitations	1968-69 Legislative Changes	Period Used in Computing Rate	Proposed Legislation
Alabama	8% 15% Over \$100,000	8% to \$10,000 15%—\$10,000 to \$100,000 No Limit Over \$100,000	8% 15% Over \$100,000	FHA/VA Loans	VA loan exempted; FHA exemption broadened to include mortgage bankers; corporate loan rate increased on loans up to \$100,000 and no limit over \$100,000. All other borrowers over \$100,000—15%.	Not clear	1) Increase rate to 15% 2) Exempt all loans over \$100,000
Alaska	10%						
Arizona	10%	18% (1½ per Month)	10%	FHA/VA Loans	Basic rate increased from 8 to 10%; Cor- porate rate increased from 1% per month to 1½% per month.	Spread over stated term	
Arkansas	10%	10%	10%	State and national banks; savings and loan associations.		Spread over stated term	Amend constitution to exempt life insurance com- pany lenders and corporate bor- rowers from in- terest limitations.
California	10%	10%	10%				UCCC
Colorado	12%	12%	12%	Licensed lenders, national and state banks, trust com- panies, savings and loan associations		Not clear	

## APPENDIX (continued)

State	Individual	Corporate	Other (Partnership, Trust, Etc.)	Exemptions from Usury Limitations	1968-69 Legislative Changes	Period Used in Computing Rate	Proposed Legislation
Connecticut	12%	12%		Mortgage Loans in excess of \$5,000.		Spread over stated term	UCCC
Delaware	8%	No Limit		FHA/VA Loans "partially" exempt		Spread over stated term	
District of Columbia	8%	No Limit				Not clear	
Florida	10%	15%				Over term of loan to date of accelera- tion.	1) Exempt FHA/ VA; 2) Exempt all loans in excess of \$100,000.
Georgia	9%	No Limit		1) All loans \$100,000 and over; 2) Corporate bor- rowers; 3) FHA/VA loans;	Exempt FHA/VA loans; increase rate to 9% on loans under \$100,000; no limit on loans over \$100,000; interest charges spread over stated term of loan.	Spread over stated term	
Hawaii	12%	12%		Industrial loans; small loan companies and banks authorized to act as such are exempt.		Not clear	
Idaho	10%	Non-agricul- tural organi- zation 12% on loans over \$10,000.				Not clear	UCCC

## APPENDIX (continued)

State	Individual	Corporate	Other (Partnership, Trust, Etc.)	Exemptions from Usury Limitations	Legislative Changes 1968-69	Period Used in Computing Rate	Proposed Legislation
Illinois	8%	No Limit	8%	1) All "Business Loans" are exempt. This includes a sole proprietor making a "business loan". 2) FHA/VA loans exempt.	Exempt FHA/VA loans; basic rate increased from 7 to 8%	Spread over stated term	Clarification of "Business Loan".
Indiana	8%	No Limit	No Limit	FHA loans made by banks and insurance companies other than life companies. FHA/VA loans exempt.	Partnerships, limited partnerships, trusts, joint ventures exempt from usury law. Increased rate from 7 to 9%	Spread over stated term	
Iowa	9%	No Limit	9%	FHA/VA loans	Increased rate from 7 to 9%	Not clear	
Kansas	10%	No Limit	10%			Not spread over stated term of loan.	
Kentucky	7%	No Limit	7%	FHA loans exempt.		Not spread over stated term of loan.	Exemption of VA Loans.
Louisiana	10% if secured by real estate mortgage; otherwise rate is 8%	No Limit	10% Same as Individual	FHA/VA Loans	Increased rate from 8 to 10%; exempted FHA/VA; provide following charges not interest: prepayment penalty, late charge, discount, service fee, commitment fee.	Not spread over stated term of loan.	

## APPENDIX (continued)

State	Individual	Corporate	Other (Partnership, Trust, Etc.)	Exemptions from Usury Limitations	1968-69 Legislative Changes	Period Used in Computing Rate	Proposed Legislation
Maine	16%	16%				Spread over stated term	
Maryland	8%	No Limit		Loans in excess of \$5,000 made to individuals for pur- pose of carrying on or acquiring a busi- ness or loan made to a business organiza- tion are exempt.	Interest and Usury Article revised 1968.	Spread over stated term	Revision and con- solidation of in- terest and usury statute.
Massachusetts	No Limit	No Limit	No Limit				
Michigan	7%	No Limit	7%	FHA/VA Loans; con- ventional home loans exempt until 12/31/70.	Removed interest ceiling on conventional home mortgages and land contracts until 12/31/70. Exempt FHA/VA Loans.	Spread over stated term	Clarification of "home loan" exemption en- acted in 1960.
Minnesota	8%	No Limit	8%	FHA/VA Loans		Spread over stated term	
Mississippi	8%	15%	8%	FHA loans made by banks, building and loan associations, credit unions, insur- ance companies.		Not clear	Exempt all FHA/ VA Loans.
Missouri	8%	No Limit	8%		Interest rate payable by Urban Redevelop- ment Corp. increased from 7 to 10%.	Spread over stated term	
Montana	10%	10%	10%	Banks have some lati- tude on installment and discounted loans.			

## APPENDIX (continued)

State	Individual	Corporate	Other (Partnership, Trust, Etc.)	Exemptions from Usury Limitations	1968-69 Legislative Changes	Period Used in Computing Rate	Proposed Legislation
Nebraska	9%	No Limit	9%			Spread over stated term	
Nevada	12%	12%	12%				
New Hampshire	No Limit	No Limit	No Limit				
New Jersey	6-8% Above 6% set administra- tively.	No Limit	6-8%	FHA/VA Loans	Permitted administra- tive increase of rate to 8%; exempts VA loans originated by mortgage companies; prohibits "points" on owner-occupied 1-4 family conventional loans.		
New Mexico	10%	No Limit	10%			Spread over stated term	
New York	5-7½% Rate set admin- istratively Presently 7½%	25%	5-7½%	FHA/VA Loans	Exempt FHA/VA loans; commitment fees charged on 1 and 2 family owner-occu- pied residences to be included in computa- tion of interest.	Spread over stated term	Increase 7½% limit.
North Carolina	8% (1st mortgage loans on real estate not exceeding \$50,000) 10% (Business property loans \$50,000 to \$100,000) 9% (Non-1st mortgage loans on real or business property in amount of \$100,000 or less) 12% (Loans over \$100,000 but not exceeding \$300,000) No Limit (Loans in excess of \$300,000)	8% 10% 9% 12% No Limit	8% 10% 9% 12% No Limit	FHA/VA Loans	Increased interest limits per loan amounts as indicated; excepted certain fees from interest computation.		

## APPENDIX (continued)

State	Individual	Corporate	Other (Partnership, Trust, Etc.)	Exemptions from Usury Limitations	1968-69 Legislative Changes	Period Used in Computing Rate	Proposed Legislation
North Dakota	8%	No Limit	8%	Business loans in excess of \$25,000; FHA/VA loans exempt.	Increased rate from 7% to 3% above current state Certificate of Deposit rate with minimum of 7%.		
Ohio	8%	No Limit	8%	Loans in excess of \$100,000.	Exempts loans in excess of \$100,000.		1) Exempt FHA/ VA; 2) Raise limit to 10%; 3) Loan interest include points or discount.
Oklahoma Oregon	10% 10%	No Limit 12%	10% 10%			Actual term of loan.	
Pennsylvania	7%	No Limit	7%	Loans in excess of \$50,000; FHA/VA Loans	Exempt loans in excess of \$50,000.	Not clear	Increase basic rate to 8%.
Puerto Rico	10%	No Limit	10%	Corporate exemption requires 12 or more stockholders			
Rhode Island	21%	21%				Spread over stated term	
South Carolina	8% to \$50,000 10%—\$50,000 to \$100,000 12%—\$100,000 to \$500,000 No Limit over \$500,000	No Limit if \$40,000 capital stock issued.	Same as individual (Includes nonprofit corpo- ration)	FHA/VA Loans	Increased rates from 7% to those indicated.		

## APPENDIX (continued)

State	Individual	Corporate	Other (Partnership, Trust, Etc.)	Exemptions from Usury Limitations	1968-69 Legislative Changes	Period Used in Computing Rate	Proposed Legislation
South Dakota	8%	No Limit	8%		Exempted profit corporations from usury limitation.	Spread over stated term	Increase basic rate to 9 or 10%.
Tennessee	10%	10%		FHA/VA Loans	Increased rate to 10%		
Texas	10%	18% (1½ month)	10%		Increased corporate rate	Not clear	
Utah	18%	18%	18%		Adopted UCCC		
Vermont	7.5%	12%	7.5%	Exempt if loan exceeds \$25,000. FHA/VA Loans can go to 12%	Increased rate from 6½ to 7½%		Exemption of loans in excess of \$50,000
Virginia	8%	No Limit	8%	FHA/VA Loans	Increased rate from 6 to 8%	Spread over stated term	
Washington	12%	12%	12%	Loans in excess of \$100,000 to corporations, Massachusetts trust, associations and limited partnerships. FHA/VA Loans	Exempt loans in excess of \$100,000 made to specified borrowers.	Spread over stated term	Clarification of \$100,000 exemption passed by '68-69 legislature.
West Virginia	8%	No Limit	8%				
Wisconsin	12%	No Limit	12%			Spread over stated term	1) Increase rate to 14%. 2) Increase allowable discount and add-on by licensed lenders.
Wyoming	10%	10%	10%	Installment loans under \$10,000.			